ARBITRATION ADVISORY

2004-01

ARBITRATION AGREEMENTS

September 22, 2004

INTRODUCTION

In recent years, an increasing number of attorney-client retainer agreements contain language providing that disputes between the attorney and the client shall be submitted to binding arbitration. Obviously such agreements, entered into at the commencement of the attorney-client relationship, precede the occurrence of a dispute. Some arbitration clauses specifically reference disputes regarding fees or costs, while others purport to deal globally with all attorney-client disagreements.

This Advisory addresses the effect of such arbitration clauses on the Mandatory Fee Arbitration ("MFA") program, specifically in light of the Supreme Court decision in *Aguilar v. Lerner* (April 22, 2004) _____Cal.4th_____(Supreme Court No. S099667) and should be read as updating Advisory 98-01, "Impact of Arbitration Clauses in Fee Agreements Upon Client's Right to Mandatory Fee Arbitration."

DISCUSSION

Agreements to arbitrate legal malpractice cases have specifically been found to be valid [*Powers v. Dickson, Carlson & Campillo* (1997) 54 Cal.App.4th 1102]. "Unless the client has agreed in writing to arbitration under this article [providing for Mandatory Fee Arbitration] of all disputes concerning fees, costs, or both, arbitration under [MFA] shall be voluntary for a client and shall be mandatory for an attorney if commenced by a client [Business & Professions Code § 6200 (c)]. Put another way, if there is an arbitration agreement between the lawyer and the client specifying that both will participate in the MFA program in the event of a dispute as to fees and costs, that agreement is enforceable under MFA. But no agreement that the arbitration as to fees or costs will be *binding* is valid unless that specific agreement is entered into *after* the dispute has arisen [Business & Professions Code § 6204(a)].

Notwithstanding these provisions, attorney-client fee agreements frequently call for

binding arbitration of all disputes without reference to MFA or to a separate consideration of disputes regarding fees and costs.

> [T]he question whether the parties' agreement to arbitrate is enforceable or is superseded by the MFAA is significant in light of the proliferation of arbitration clauses in attorney retainer agreements during the last two decades. This proliferation is understandable, for we have presided over a recent period of rapid expansion of arbitration as a dispute resolution mechanism [*Aguilar v. Lerner*, supra, ____Cal.4th_____(S099667, slip opinion p. 10)].

It therefore seems well established that lawyers and clients are free to enter into agreements for binding arbitration of future disputes with the sole exception of potential disputes regarding fees or costs governed by the MFA system and Business & Professions Code § 6204 in particular. The MFA statute gives the client the absolute right to insist upon arbitration - either advisory or, if all parties agree, binding - under Business & Professions Code §§ 6200 *et seq*. The conundrum, however, is how to apply arbitration agreements which either (a) fail to separate out disputes over fees and costs or (b) provide that the client's rights to MFA arbitration of fees and costs are preserved but - if non-binding MFA arbitration is elected - any subsequent resolution must be through binding arbitration rather than through access to court or jury trial.

Alternative Systems, Inc. v. Carey, (1998) 67 Cal. App.4th 1034, held that the Mandatory Fee Arbitration statute preempted a binding private arbitration clause in a fee agreement if the arbitration provision purported to govern disputes as to fees and costs. The client in *Alternative Systems* invoked his rights under MFA and was entitled to a trial *de novo* under the MFA scheme. The court concluded that after non-binding MFA the client retained the right to access the courts rather than being required by the arbitration agreement to submit the dispute as to fees or costs to subsequent binding arbitration [*Id*., at 1044].

In *Aguilar v. Lerner*, the plaintiff (himself an attorney) hired counsel in a marital dissolution and signed a written contract containing an agreement to binding arbitration of any dispute "concerning fees . . . or any other claim . . ." against his attorney. When a dispute arose, the plaintiff filed a malpractice action against his since-discharged attorney; the attorney cross-complained for fees and costs and petitioned to compel arbitration under the terms of the agreement. Plaintiff contended the arbitration agreement was invalid since, on its face, it contravened the MFA, in particular Business & Professions Code § 6204, having been entered into before the dispute arose. The superior court granted the petition to compel arbitration and further ordered that arbitration would be binding. Plaintiff lost his malpractice claim and was also on the receiving end of an arbitration award for fees and costs in favor of his former counsel [*Aguilar v. Lerner*, supra, slip opinion pp. 3-4].

The *Aguilar* court discusses at length the differences between the California Arbitration Act ("CAA") [C.C.P. §§ 1280 *et seq.*] generally and the mandatory fee arbitration program which represents "a separate and distinct arbitration scheme" [Slip opinion p. 6]. The court noted two important distinctions between MFAA and CAA arbitration. First, "the obligation to arbitrate under the MFAA is based on a statutory directive and not the parties' agreement."

Secondly, "whereas a client cannot be forced under the MFAA to arbitrate a dispute concerning legal fees, at the client's election, an unwilling attorney can be forced to do so."

According to the majority opinion, "[i]n light of plaintiff's waiver, we have no occasion to address how we might reconcile a client's rights under the MFAA with a client's pre-existing agreement with counsel to arbitrate under the CAA" [*Aguilar v. Lerner*, supra, slip opinion p. 2]. The concurring opinion concludes that, insofar as *Alternative Systems* promises access to the courts in the face of an agreement to submit all attorney-client disputes to binding arbitration, it "cannot survive today's ruling" [*Aguilar v. Lerner*, supra, concurring opinion by Chin, slip opinion p. 5].

It must be anticipated that parties seeking to enforce binding arbitration agreements may, after participating in MFA at the request of a client, insist that any *de novo* review be done in the arbitral forum designated in the private arbitration agreement. This raises the question whether MFA program arbitrators should treat such disputes any differently than fee disputes not involving private arbitration agreements. The Committee recommends that until a more definitive determination of whether *Alternative Systems* has been overruled is announced, it be presumed that *Alternative Systems* is in fact still the applicable law. In crafting arbitration awards where one party maintains that there is a binding arbitration agreement, it is best to keep in mind that the California MFA scheme provides only for arbitration of disputes involving fees and costs, not resolution of other components of disputes or claims between an attorney and a client. The local programs authorized under the State Bar auspices by the MFA are not constituted to resolve ancillary matters such as malpractice claims unless separately constituted and operated by a local bar association electing also to offer services pursuant to private arbitration agreements (as occurred in *Aguilar*). Thus, while an award may well choose to recite the existence of a dispute of the type considered in *Alternative Systems*, it should be left for a subsequent reviewing court or arbitrator(s) to determine if trial *de novo* before a court is permitted. Moreover, irrespective of whether *Alternative Systems* continues to remain good law, program administrators should continue to advise parties of their *de novo* rights under the existing program law and rules as before.

Another problem raised by *Aguilar v. Lerner* concerns the interplay between the California MFA program and the Federal Arbitration Act (FAA) [9 U.S.C. §§ 1 *et seq*]. The court offers the comment in n. 8, slip opinion p. 16, "Because neither party has raised it, we decline to address any issue concerning the Federal Arbitration Act (9 U.S.C. § 1)." The pre-emptive effect of the FAA on state arbitration law generally is a much litigated and still somewhat unsettled area [See e.g., *Hedges v. Carrigan* (2004) 117 Cal.App.4th 578, 583-586]. Since there are many instances where the subject matter for which attorneys are retained may have interstate commerce ramifications, we must anticipate that parties seeking to enforce binding arbitration agreements may seek to invoke the FAA in support of their positions. The Committee recommends that MFA program arbitrators not attempt to become involved in the resolution of this issue but instead hear and decide fee and costs disputes without reference to the FAA.

CONCLUSION

In general, *Aguilar v. Lerner* should not significantly alter the mandatory fee arbitration landscape. The filing of a legal action by the client against the attorney still ousts the MFA program of jurisdiction over a fee dispute. It is the recommendation of the State Bar Committee on Mandatory Fee Arbitration that - unless and until contrary guidance is provided by a court of competent jurisdiction - when confronted with what appears to be a binding arbitration agreement in an attorney-client fee contract, arbitrators continue to follow the holding in *Alternative Systems, Inc. v. Carey* [(1998) 67 Cal.App.4th 1034], and continue to issue *non-binding* arbitration awards in the absence of post-dispute stipulations making such awards binding, and continue to advise the parties of their available rights to trials *de novo* following nonbinding arbitration. With respect to the relationship between the Federal Arbitration Act and California MFA, again unless and until a competent court directs otherwise, the Committee recommends that arbitrators consider the California statutory scheme to be an acceptable dispute resolution program even in arbitrations which may have interstate commerce overtones and that MFA programs continue to be guided by the MFA statutes and rules.